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UNCLAS SECTION 01 OF 02 ABUJA 001048

SIPDIS

DOE PASS TO CAROLYN GAY

E.O. 12958: N/A
TAGS: ECON EFIN ELAB ENRG EPET PGOV PREL NI
SUBJECT: FUEL SUBSIDIES IN NIGERIA: BETWEEN A ROCK AND A HARD PLACE

REF: ABUJA 1012

¶1. (U) SUMMARY: Up until April or May, the Nigerian National Petroleum Company (NNPC) received an allocation of petroleum from the GON at below-market rates, sold part of it on world markets, and used the rest to subsidize gasoline prices domestically, all outside the government's formal budget. In April the GON started selling to the NNPC at international market rates, thereby ending the subsidy. If strikers are successful at getting the price of gasoline down to 38 Naira per liter, the NNPC would be required again to subsidize the domestic price of gasoline, and the continuation of subsidies "off the books" through NNPC would become unsustainable. The GON would be left with the choice of either backpedaling its economic reform program and subsidizing gasoline through the formal federal budget, which currently has no allocation for this, or else make gasoline prices subject to market forces. END SUMMARY.

¶2. (U) At the heart of the current strike in Nigeria over rising fuel prices is the issue of the subsidization of gasoline prices. The GON for years has effectively subsidized the price of fuel through the Nigerian National Petroleum Company (NNPC), yet none of this subsidy appears in the federal budget.

¶3. (U) The subsidy operation has been conducted by the GON selling a domestic allocation of crude oil to the Nigerian National Petroleum Company (NNPC), a parastatal, at a lower-than-market price, currently estimated at USD 25 per barrel. The allocation, roughly equal to Nigeria's assumed domestic demand, is approximately 445,000 barrels per day.

¶4. (U) Although its allocation for domestic consumption is 445,000 bpd, NNPC has the refining capacity for only around 200,000. Most of the remaining 245,000 bpd appear to have been sold abroad at market rates.

¶5. (U) Normally, when crude petroleum is sold abroad above the federal government's budgeted price of USD 25, any revenues above that are considered "excess revenues" and are sterilized, being deposited in a special account at the Central Bank of Nigeria (CBN). This is not true, however, for crude petroleum from Nigeria's domestic allocation that NNPC sells abroad. Because in this case it is not the GON selling the crude abroad, but rather a parastatal, the "excess revenue" above USD 25 per barrel that NNPC earns is not reflected in the federal budget and therefore is not deposited in the federal government's "excess revenue" account. If we assume a purchase price from the GON of USD 25 per barrel and a sales price on international markets at USD 35 a barrel. Up until recently, this could have meant an annual profit for NNPC of roughly USD 900 million.

¶6. (U) The profit on the sale abroad of crude petroleum earmarked for domestic consumption gave NNPC a war chest with which to purchase gasoline abroad and subsidize its low wholesale price. The landed price of gasoline in Nigeria is currently around N 50 per liter, and NNPC has been selling it wholesale to marketers at N 38.5 per liter. The National Labour Council (NLC) is demanding (reftel) that the price at the pump be reduced to around N 38. At that rate, marketers tell us that NNPC will have to sell it to them at N 33.5 per liter in order for them to clear their transportation and marketing margins. According to Wale Tinubu, Managing Director of Oando (formerly Unipetrol), a downstream petroleum products marketing company, as quoted in an interview with Olusegun Adeniyi in THISDAY Newspaper on Thursday, June 10, 2004, NNPC's subsidies of gasoline during the past five months were as follows:

January -	N 194,907,861 per day (USD 1.43 million)
February -	N 223,721,904 per day (USD 1.65 million)
March -	N 221,913,871 per day (USD 1.63 million)
April -	N 370,732,860 per day (USD 2.73 million)
May)	N 460,438,839 per day (USD 3.40 million)

(Exchange rate used is N 136 to USD 1)

¶7. (U) Taking the average of this, we get USD 2.168 million per day in subsidies, or USD 780 million on an annualized basis, spent on subsidies.

¶8. (U) Nigeria's consumption of refined petroleum products is estimated at around 30 million liters a day. This breaks down approximately as 60% gasoline, 20% diesel, 15% kerosene and 5% other. The landed cost of imported gasoline is currently around N 50, and the NLC is insisting that the price of gasoline be reduced to N 38 per liter, effectively forcing the NNPC to either subsidize it at N 12 per liter or, for gasoline refined in Nigeria, forgo the extra profit that NNPC could have realized had they sold it at international market rates. If we assume that all refined petroleum products carry a subsidy of N 12 per liter (N 50 landed price minus N 38 sales price), then this amounts to an effective subsidy of USD953 million per year going forward. By way of comparison, the entire budgetary revenue of the Nigerian government for 2004 is N 1,303 trillion (USD 8.25 billion).

¶9. (U) As part of its economic liberalization, the GON began selling crude to NNPC at world market prices in April and announced this policy publicly in May. In May, NNPC reduced its the number of credit days for its sales from 30 to 15, and Nigerian media reported NNPC Group Managing Director Funsho Kupolokun on Monday, June 7 as saying that if NNPC continued to buy crude at market rates and subsidize the price of gasoline, the company would soon be "kaputt."

¶10. (U) Ulu Akani, Senior Technical Advisor to Kupolokun, confirmed to Econoffs on June 10 that NNPC was purchasing crude petroleum from the GON at market rates. He further noted that the 200,000 bpd that are refined in Nigeria are being sold at below their cost of production.

¶11. (U) Attempts to reach Embassy contacts at the MOF to reconcile the difference between NNPC's allocation of 445,000 bpd and Nigeria's refining capacity of 200,000 bpd were unsuccessful.

¶12. (U) Comment: So far, the GON economic team appears to be serious in its efforts to deregulate the downstream petroleum sector, unbundle the NNPC and privatize its downstream subsidiaries. NNPC will not be able to resume the off-the-books subsidy indefinitely if the government does restore the fuel subsidy. The choices are either to go back to the status quo ante, incorporate subsidies into the formal federal budget, or lift all subsidies and face the political consequences.
CAMPBELL